

**Facebook****(FB: NNM; \$32.00)****Hold | Target: \$NA**

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rory@capstoneinvestments.com**FB: INITIATE WITH HOLD; STRONG DISPLAY W/NEW BUSINESS POTENTIAL, BUT FAIR VALUED**


- **Good Company, Fairly Valued Stock Leads To Hold.** We believe Facebook's core display business could generate growth rates that exceed overall industry display growth, but the FB shares' current 24X 2013E EV/EBITDA multiple assumes significant growth from new businesses when the Company hasn't yet optimized its core display business. In particular, indications the past year that the Company's premium ad products are not performing as well as advertisers would like lead us to believe that until this issue is fixed a premium multiple is not warranted.
- **\$16B Offering.** Facebook offered 421M shares at \$38/share to the public on May 18 2012. We estimate the offering was valued at 30X 2013E EV/EBITDA.
- **Strong User Growth To Date.** Facebook surpassed 900M monthly active users (MAU) in 1Q12 and 526M daily active users – 30% Y/Y growth. We believe 35% of the global Internet population is on Facebook suggesting upside, all things being equal.
- **Increased Share Of Display Budgets The Past Few Years.** Over the past couple quarters we spoke extensively with agencies, CMOs, and SEM agencies that represent over \$30B in adspend and believe Facebook has increased its share of online display budgets to 5%-10% from zero just a couple years ago.
- **But Lack Of New Premium Ad Products Weighs On Growth.** Facebook released a new sponsored story unit in 1Q12 that did not address large advertisers' demands for more specific ROI info. As a result, we believe an increasing number of advertisers are spending budgets on less expensive self-serve inventory that otherwise would have been spent on premium inventory, putting pressure on CPMs and revenue growth. We believe this trend will continue until better premium ad products are released and don't see many indications of new products reversing this trend soon.
- **Large Mobile Audience.** Facebook grew its mobile audience to 488M in 1Q12, almost 50% of total users. In addition these users are twice as active as PC users, benefitting time spent on the site.
- **ROI On Mobile Likely Weak Initially.** On the roadshow management indicated it would invest significantly this year in mobile as more of its users shift to that platform. In addition, we have heard that the recently launched mobile ad unit has been slow to attract spend out of the gates and expect advertisers to stick with more traditional mobile ad units the next year. As a result, we believe mobile could weigh on margins into 2013.
- **Credits Growing As Revenue Driver, We Wouldn't Be Surprised To See A Payments Business.** Credits increased from 5% of revenue in 2010 to 18% in 1Q12 after Facebook required developers to use it for sales of virtual goods over independent providers. We believe the Credits product could be expended to process payments across third-party sites in the future.
- **30% Revenue Growth, Modest Margin Improvement.** We forecast 38% revenue growth in 2012 and 32% revenue growth from '12E through '16E. We forecast EBITDA margins of 53% in 2012E, increasing to 55% by 2016E. We expect large stock-based compensation to drive an earnings loss in 2Q12E on a GAAP basis, but expect the Company to earn \$0.18 in diluted EPS for the full year 2012 and \$0.76 in diluted EPS ex-SBC.

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Rating	HOLD	PF Earnings Per Share							
Target Price	NA	FYE - December							
Ticker Symbol	FB		2010A	2011A	2012E	2013E			
Market	NASDAQ	1Q - March	NA	\$	0.10	\$	0.13	NA	
Stock Price	\$32.00	2Q - June	NA	\$	0.13	\$	0.29	NA	
52 wk High	\$45.00	3Q - Sept	NA	\$	0.13	\$	0.15	NA	
52 wk Low	\$31.00	4Q - Dec	NA	\$	0.16	\$	0.19	NA	
Shares Outstanding:	2,361.0 M	Year	NA	\$	0.52	\$	0.76	\$	0.68
Public Market Float:	421.0 M	P/E	NA		62.1x		42.1x		47.3x
Avg. Daily Volume	371,000,000	Revenue (\$M)	\$1,974.0		\$3,711.0		\$5,118.3		\$6,756.1
Market Capitalization:	\$75,552 M	EV/Sales	32.9x		17.5x		12.7x		9.6x
Institutional Holdings:	NA								
		Common Institutional Ownership Profile (9/30/11)							
Senior Executives		Shareholder	Shares ('000)			% of Total			
Mark Zuckerberg	CEO								
Sheryl Sandberg	COO								
David Ebersman	CFO								

Capitalization			Not enough data to form a chart
Market Value Basis (\$M)	5/24/2012	%	
Long-Term Debt	\$0	0.0%	
Plus Market Value of Equity	75,552	116.4%	
Less Cash:	10,667	16.4%	
Enterprise Value	\$64,885	100.0%	
Book Value Basis ('000)	3/30/2012	%	
Long-Term Debt	\$0	0.0%	
Other Liabilities	0	0.0%	
Book Value of Equity	12,354,000	100.0%	
Total Capital	\$12,354,000	100.0%	

Source: Company reports, Big Charts and CapStone Investments estimates.

Company Description

Facebook's mission is to give people the power to share and make the world more open and connected. Over 900M people use Facebook every month to keep up with friends, upload an unlimited number of photos, share links and videos, and learn more about the people they meet.

Table Of Contents

Advertiser Survey.....	4
Proprietary Share Tracker Illustrates User Reach.....	5
Offering Summary.....	7
Monopoly On People's Time Leads To Revenue Opportunities.....	8
Strong User Growth, Moderating As Base Matures.....	9
Large Mobile Audience, Largely Untapped.....	10
Lack Of New Premium Ad Products Could Be Driving Decelerating Revenue Growth.....	11
New Sponsored Story Unit Increases ROI, Drives Mobile.....	12
Instagram Acquisition Boosts Mobile.....	13
Needs To Find Another Homerun Beyond Display Ads.....	14
Premium Ads – Sponsored Stories & Engagement Ads.....	15
Run-Of-Network Ads – Marketplace Ads.....	16
Credits/Payments – Small, But Growing.....	17
Revenue Opportunities Outside The Facebook Platform.....	17
Strong Growth, Modest Margin Improvement, Fairly Valued Stock...	18



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